

BEFORE
THE PUBLIC SERVICE COMMISSION OF
SOUTH CAROLINA
DOCKET NO. 2018-82-S

IN RE:)
)
Application of Palmetto Wastewater)
Reclamation LLC for adjustment of rates)
and charges for, and modification to certain)
terms and conditions related to the)
provision of sewer service.)
_____)

PREFILED REBUTTAL TESTIMONY OF BRYAN D. STONE
ON BEHALF OF PALMETTO WASTEWATER RECLAMATION LLC

Q. ARE YOU THE SAME BRYAN D. STONE WHO HAS PREFILED DIRECT TESTIMONY
IN THIS MATTERS?

A. Yes, I am.

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY IN THIS
PROCEEDING?

A. The purpose of my rebuttal testimony is to respond on behalf of Palmetto Wastewater Reclamation LLC, or “PWR,” to the position taken by the South Carolina Office of Regulatory Staff, or “ORS,” with respect to the application for rate relief in this proceeding. As the Commission is aware, PWR’s application seeks an increase of \$6.68 in its residential sewer rate, which would produce a rate of \$41.18 per single family equivalent, or “SFE,” per month.

Q. WHAT IS YOUR UNDERSTANDING OF ORS’S POSITION?

16 A. My understanding is that ORS wishes to limit PWR's increase to only \$1.19 per
17 SFE, instead of the \$6.68 per SFE that PWR seeks in its application. So, ORS is
18 recommending an 82% reduction of PWR's requested increase in its application. This
19 would result in a rate of \$35.69 per SFE (3.45% increase over current rate) instead of the
20 \$41.18 per SFE (19.38% increase over current rate) sought by PWR. I understand that
21 ORS reaches this small increase to the rate by adjusting PWR's proposed expenses, rate
22 base and revenues and by reducing PWR's proposed return on equity ("ROE"). If adopted
23 by the Commission, these ORS adjustments and reduction will result in additional revenues
24 of only \$114,516. This does not reflect the effect of the additional rate case expenses which
25 have been and will be incurred since ORS completed its audit. ORS witness Anthony
26 Sandonato contends that this greatly reduced amount of additional revenue is "in the public
27 interest."

28 **Q. DO YOU AGREE WITH MR. SANDONATO'S CONTENTION?**

29 A. No, I do not.

30 **Q. PLEASE EXPLAIN WHY YOU DO NOT AGREE.**

31 A. As is reflected in the rebuttal testimonies of Mr. Daday and Mr. Walker, PWR
32 disagrees with some of the adjustments proposed by ORS's internal witnesses and the
33 recommendation of its outside consultant, Mr. Parcell, regarding an appropriate ROE. If
34 the Commission were to accept any or all of the adjustments and ROE proposed by ORS,
35 the resulting rate is not in the public interest as Mr. Sandanato contends. Furthermore, the
36 ORS recommendation fails to consider the utility's right to earn a fair return, which is a
37 right the Commission should, independent of ORS, balance with the customer interest
38 when determining if the proposed rate is in the public interest.

39 **Q. WHY IS THE RESULTING RATE NOT IN THE PUBLIC INTEREST?**

40 A. There are two reasons why this is the case. First, ORS's recommendation does not
41 correctly apply the plain language of the statute it relies upon for this contention. Second,
42 the public interest cannot be served when the financial fair treatment of the utility is
43 ignored.

44 **Q. WOULD YOU PLEASE ELABORATE ON THE FIRST OF THESE TWO POINTS?**

45 A. Yes. Mr. Sandanato correctly states in his testimony that the "public interest" of
46 the State of South Carolina that ORS is charged with representing under South Carolina
47 Code section 58-50-10 is defined to mean:

48 "the concerns of the using and consuming public with
49 respect to public utility services, regardless of the class
50 of customer, and preservation of continued investment
51 in and maintenance of utility facilities so as to provide
52 reliable and high-quality utility services."
53

54 Thus, the legislature has included two specific components within this statutory charge
55 which ORS must consider in making its recommendations to the Commission: 1) the
56 interests of customers with respect to their utility services, and 2) the State's interest in
57 promoting investment in and maintenance of utility systems so that reliable and high-
58 quality service can be provided. The rates recommended by ORS do not properly consider
59 either component.

60 **Q. HOW CAN YOU SAY THE CUSTOMER INTEREST COMPONENT OF THE STATUTE**
61 **IS NOT PROPERLY CONSIDERED IN ORS'S RECOMMENDATION GIVEN THAT IT**
62 **RESULTS IN AN 82% DECREASE IN THE RATE REQUESTED?**

63 A. I can say that for several reasons. First, Mr. Sandanato's recommendation
64 implicitly assumes that the only concern of the using and consuming public is in lower
65 rates, which is not a correct assumption. The statute encompasses all aspects of customers'
66 utility services and recognizes that it is desirable that customers have reliable and high-
67 quality service. Customers understand that such service comes at a cost, and PWR believes
68 that its customers have signaled that a rate higher than that recommended by ORS is
69 reasonable in view of PWR's costs and investments to ensure that customers have a reliable
70 and high-quality service.

71 **Q. WHAT BASIS DO YOU HAVE TO ASSERT THAT CUSTOMERS WOULD ACCEPT AS**
72 **REASONABLE A RATE HIGHER THAN THAT PROPOSED BY ORS?**

73 A. This is demonstrated by the fact that, as of the date of this testimony, no customer
74 has filed a protest letter with the Commission opposing the proposed monthly service rate
75 of \$41.18 per SFE, which is slightly more than a 19% increase. This is highly unusual.
76 Nor has any customer requested a public hearing. I think this is also noteworthy. Mr.
77 Sandanato's direct testimony reflects no issues with the quality of PWR's utility service or
78 customer service. In fact, he does not even mention customer complaints to the
79 Commission or PWR regarding our services. Appropriately, he acknowledges that PWR is
80 in full compliance with the Commission's regulations and that there have been no
81 environmental events reportable to the Department of Health and Environmental Control
82 ("DHEC") during the relevant period. We submit that these facts demonstrate an
83 exemplary level of utility service and performance. However, achieving that level of
84 service and performance did not happen by accident; it happened only by a consistent
85 commitment on the part of PWR. That commitment is manifested to a great degree in

PWR's investment in its facilities. This includes approximately \$6.8 million of capital improvements since PWR's last rate relief proceeding. These were needed to refurbish the Alpine and Woodland systems which were in a poor state of repair, and to bring them into regulatory compliance. This amount is in addition to the approximately \$6 million that PWR had previously invested in these two systems to bring them up to the standards required by DHEC as contemplated in the PWR's memorandum of understanding with DHEC, which is referenced in the testimony of Mr. Daday.

Q. YOU STATED THAT THE SECOND COMPONENT OF THE STATUTE RELIED UPON BY MR. SARDANATO WAS ALSO NOT CONSIDERED IN THE ORS RECOMMENDATION; WOULD YOU PLEASE EXPLAIN THAT STATEMENT?

A. Yes. As I note above, the statute requires that ORS consider continued investment in utility facilities so as to enable PWR to provide reliable and high-quality utility services. The ORS's position actually serves to discourage any future investment in facilities by PWR – or any of the other utilities affiliated with PWR, such as the much larger Palmetto Utilities.

Q. WHY IS THAT THE CASE?

A. If the ORS recommendation is accepted by the Commission, PWR will be in a demonstrably worse financial position after it has made the \$6.8 million facilities investment than it was following its last rate relief proceeding. This can be seen in the audit exhibits to ORS witness Seale's direct testimony which reflect that, if ORS's position is adopted, the resulting operating margin would be 14.75%. This operating margin would be approximately 13% lower than the 17.07% operating margin previously allowed by the Commission for PWR.

109 Additionally, as shown in the exhibit attached to the rebuttal testimony of company
110 witness Daday, PWR's ad valorem taxes have increased by approximately \$350,000 as a
111 result of PWR's \$6.8 million investment. The ORS recommendation of only a \$1.19 rate
112 increase would allow PWR to generate additional revenues of less than one-third of the
113 amount of that tax increase. When the recommended increase in annual revenue does not
114 cover even a third of the Company's additional ad valorem taxes, it makes any investment
115 illogical and makes investment going forward prohibitive.

116 Furthermore, ORS proposes that PWR's monthly residential service rate increase
117 only 3.45% from that set by the Commission in 2014. However, the cumulative rate of
118 inflation since PWR's last rate relief proceeding (per ORS witness Parcell at page 12, ll. 7-
119 9) was 7.1%.

120 In sum, ORS's recommendation to the Commission is that a utility which (1) does
121 not generate a notable number of customer complaints, (2) provides a level of customer
122 and utility service which complies with all Commission regulations, (3) is environmentally
123 responsible, (4) has demonstrated its commitment to making needed investments in quality
124 system facilities, and (5) has received no filed opposition from its customers to a requested
125 19% rate increase, should have rates approved which provide an increase that results in (a)
126 a significantly lower operating margin than previously permitted by the Commission, (b)
127 additional revenues which do not cover the cumulative rate of inflation since its last rate
128 proceeding, and (c) the realization of two-thirds less revenue than is required to cover the
129 property tax on a \$6.8 million additional investment. Far from promoting continued
130 investment in PWR's facilities, the ORS recommendation is a disincentive for PWR or its
131 parent to make any further investments in its systems located in the State of South Carolina.

We do not think that is what the General Assembly envisioned and therefore do not think that ORS has properly considered the second component of its statutory charge to represent the public interest of South Carolina in making its recommendation in this case.

Q. YOU STATED THAT THE PUBLIC INTEREST STANDARD REFERENCED BY MR. SARDANATO IS NOT THE STANDARD BY WHICH THE COMMISSION SHOULD DETERMINE A JUST AND REASONABLE RATE FOR PWR; WOULD YOU PLEASE EXPLAIN THAT STATEMENT?

A. The standard under the statute relied upon by Mr. Sardanato applies to ORS's representation of the State in ratemaking matters before the Commission. It does not establish a standard by which the Commission is required to determine just and reasonable rates. PWR believes that the public interest is only achieved by a Commission determination that balances the interests of customers with the constitutional right of a utility to earn a fair return on its investment as discussed in the testimony of Mr. Walker. Because the statute referenced by Mr. Sardanato does not include any requirement with respect to the utility's right to earn a fair return, the Commission cannot rely on the ORS recommendation. The Commission should, independent of ORS, determine what is in the public interest through a balancing of the interest of customers and utility's right to a fair return.

Q. DOES THE ORS RECOMMENDATION RESULT IN RATES WHICH ARE JUST AND REASONABLE UNDER THE PUBLIC INTEREST STANDARD APPLICABLE TO THE COMMISSION'S DETERMINATION OF THE PUBLIC INTEREST?

A. No, it does not. A return on a \$6.8 million investment in assets which does not generate additional revenue sufficient to cover additional property taxes that have to be

155 paid on the new assets is not a fair return on the investment. Mr. Walker's testimony
156 explains why the return on equity recommendation of ORS witness Parcell is wrong from
157 an analytical standpoint. But it is apparent that no reasonable investor would ever devote
158 resources to an investment which basically does not recover the property taxes created by
159 its asset acquisitions and does not generate revenues which even match, much less exceed,
160 the cumulative rate of inflation over the time periods in which the capital acquisitions are
161 made. In short, no reasonable investor will make a risky investment in which the best case
162 is a negative return in real dollars. The Commission should recognize that the ORS
163 recommendation does not in any way serve the public interest standard applicable to the
164 Commission's determination in this matter because it wholly ignores the Company's right
165 to recover its expenses and earn a reasonable return on its investment.

166 **Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?**

167 **A** Yes, it does.